IN THE

Supreme Court of the United States

OCTOBER TERM, 1946.

No. 847.

THE UNITED STATES, *Petitioner*,

v.

THE MUNSEY TRUST COMPANY OF WASHINGTON, D. C., *Receiver*.

On Writ of Certiorari to the Court of Claims.

BRIEF FOR RESPONDENT.

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INDEX.

CITATIONS.

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OPINION BELOW.

The opinion of the Court of Claims (R. 17-28) is reported in 67 F. Supp. 976.

JURISDICTION.

Petitioner has invoked the jurisdiction of this Court under section 3 (b) of the Act of February 13, 1925, as amended. The judgment of the Court of Claims was entered on October 7, 1946. (R. 28). The writ was granted on March 3, 1947 (R. 29).

QUESTION PRESENTED.

A statute[1] requires that before an administrative agency of the United States shall award any contract for the construction, alteration or repair of any public building or public work, it shall take, and the contractor shall give, bonds with surety, conditioned for the performance of the work and for the protection of all persons supplying labor and material in the work. Is it not implicit in the whole transaction that the contract price shall not be invaded by the United States for the satisfaction of its wholly *unrelated* and independent claims against the contractor to the damage of the surety which has performed the contractor's obligation, both to the United States and to the furnishers of labor and material by paying the latter?

STATEMENT.

It should be observed that the bid for work at the St. Louis Post Office was not made until subsequent to the making of the contracts which the surety bonded, (R. 15, 13) and as a consequence the independent claim based on that transaction did not arise until after the giving of the bonds here involved. The deposit taken by the Government in the amount of $415.00 to secure the bid of $20,743.00 for painting the St. Louis Post Office, is in the amount of approximately 2% and appears to be grossly inadequate.

In making its settlement, the General Accounting Office proceeded in total disregard of the surety's rights. In the cases of three of the contracts[2] (R. 16) the General Accounting Office paid over to the receiver the full contract balances although payments by the surety in each instance were less than those balances (R. 17).

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[1] Miller Act, 40 U. S. C. 270a, et seq., App. pp. 25-26.

[2] Whitewater, Wisconsin
Portland, Maine
Skowhegan, Maine

ARGUMENT.

Summary of Argument.

1. The contract for the work and the bonds required by the Government in connection therewith impose upon the contractor the obligation of paying all furnishers of labor and material. When the contractor fails to make such payment, he breaches his contract and bond just as much as though he had failed to execute the work. When the contractor breaches his contract, he is not entitled to receive further payments under it. When the surety pays labor and material furnishers, it is performing the contract and answering under the bond by discharging the obligation which it assumed both to the Government and to supplymen. The contract balances are earned by it and belong to it.

2. The Government's rights of off-set are equitable in nature. They have never been prescribed by statute. There is an absence of mutuality between the debts in this case. The debt due to the Government concerns the contractor alone. The debt owed by the Government is primarily an obligation running to the surety as a consequence of its performance of the contract requirements.

3. In innumerable cases which have arisen in the Federal Courts over the last fifty years involving the disposition of such contract proceeds, the courts have awarded them to the surety which either completed the work or paid furnishers of labor and material. This has been done on the basis of such equitable rules as were conveniently applicable to the particular case. It has been held that the surety was subrogated to the rights of the Government. In other cases the surety has been held to be entitled to subrogation to the rights of the furnishers of labor and material. In a few cases subrogation to the contractor's rights in the fund was the ground of decision; but these cases are rare because the contractor's rights to the fund

ordinarily become so far subordinate by the time of the contest, that they are worthless. The fund has also been held subject to an equitable lien in favor of furnishers of labor and material and such suppliers have been allowed to maintain an action in their own name to satisfy their claims against it.

4. Various contentions of the Government's brief—that allowance of an off-set will result in greater convenience as a matter of procedure, that the receiver succeeded to no more than the contractor's claim against the United States, that subrogation must be denied because the debt is not yet paid, that the making of off-sets is a well established administrative practice, are all shown to be inapplicable to the situation in the case at bar.

1. The Surety Has a Legal Right to the Contract Balances.

The Court of Claims decided this case upon the basis of equitable rules which have developed in a vast body of cases since the decision of *Prairie State National Bank* v. *United States*, 164 U. S. 227. The case will bear a more direct analysis. The whole implication of the transaction is that *the contract proceeds were to form the means of carrying out the project* and that they were to be available to the contractor, to the surety, and to the Government for that purpose. In entering into the transaction, the Government assumed to the surety an obligation not to defeat this purpose by diversion of the contract funds for its own private convenience. It has no right to appropriate the contract funds for the satisfaction of unrelated indebtedness of the contractor to it. Respondent is content to present the case upon this ground alone. Discussion of equitable rules applied in this field is included to show the extent to which development in those lines is in complete accord with the notion that the Government has such a direct legal responsibility.

When the contractor failed to pay its bills for labor and material furnished in the performance of the contract, it

breached not only the bond, but the contract as well. In *Martin v. National Surety Company*, 300 U. S. 588, the surety on a bond given under the prior[3] statute sued to impound the contract proceeds for its indemnity and exoneration from labor and material claims made against it. The last progress payment had been collected by Martin, the assignee of the contractor, while the retained percentages were in the hands of the Government. In awarding the contract balances to the labor and material furnishers, in whose favor the surety withdrew on becoming insolvent, this Court said, at pp. 593-4:

> "The proceeds of the contract, when collected by Martin under his power of attorney, were received by him with knowledge of the agreement between the contractor and the surety whereby such proceeds became a fund to be devoted in the first instance to the payment of materialmen and others similarly situated. In our view of the law, the equities in favor of materialmen growing out of that agreement were impressed upon the fund in the possession of the Court."

At p. 595:

> "The contractor undertook that materialmen would receive their money promptly while the work was going on. In failing to pay them, he violated a duty to them, but a duty also to the Government, for the default was a breach of the condition of the bond. If the assignment to the surety creates a lien upon the fund, the contractor will be compelled to fulfill the duty thus assumed."

And again, at pp. 597-8:

> "But the statute directs that a bond for the prompt payment of materialmen and laborers shall be executed by the contractor before the commencement of the work. Not only that, but the contract with the Government, which was drawn in the standard form, is a confirmation and adoption of the statutory duty. The

[3] 40 U. S. C. 270 etc., App. p. 26.

terms of the bond are read into the contract, and there is default under the contract when there is default under the bond."

As a consequence of the default of the contractor in the payment to furnishers of labor and material, it forfeited its right to receive payment under the contracts. It was not until the surety remedied this breach by coming forward and paying these claims, that the contract balances became payable. It would be a strange result, if the surety's payment of labor and material bills had the effect of enabling the Government to apply to its own independent claims against the contractor, the funds thus freed from the penalty of the breach. The contract and bond contemplated not only that the work would be done, but also that labor and material bills would be paid as well. The failure to do either was a breach of the contract and of the bond which was required both by the statute and the contract. The surety mends the breach as much by paying labor and material claims as it does by performing the work. There can be no question but that if the surety had completed the work it would be entitled to so much of the remaining contract balance as would be necessary to exonerate or indemnify it from loss. *United States Fidelity & Guaranty Co.* v. *United States*, 92 C. Cls. 144. The reason for this is that if the surety does not elect to complete the work,[4] and the Government itself completes, the measure of damages chargeable to the contractor and the surety is only the excess cost of completion after first making allowance for the credit represented by the unpaid balance of the contract price. *Lacy* v. *Maryland Casualty Co.*, 32 F. (2d) 48 (C. C. A. 4th); 16 Comp. Dec. 351; 26

[4] The bonds taken by the United States are for the payment of a sum of money. The obligation of the bond is discharged by the performance of its condition (R. 14). The surety does not agree to perform the work, but to be answerable in damages for non-performance. Not infrequently the surety actually undertakes the completion of a defaulted contract in order to minimize the damage which ordinarily follows.

Comp. Dec. 467; 8 Comp. Gen. 58; 8 Comp Gen. 435. No different result should follow where the breach consists of a failure to pay furnishers of labor and materials, and the surety comes forward and pays them.

It is obvious that the Government, the contractor, and the surety all contemplated that the contract funds were to be available to the contractor for the purpose of executing the work. Execution of the work necessarily includes payment for labor and material. This is demonstrated by the provisions of the standard form of Government contract which authorize payment to the contractor in installments as the work progresses with an amount, usually 10 per centum, to be withheld until completion and acceptance of the work. Material departures from the contract terms by the party secured would release the security of the bond by affording the surety the defense that its obligation was altered without its consent. Here the surety is entitled to insist upon performance by the Government through payment by the Government of so much of the contract balances as will prevent an enlargement of its obligations under the bonds.

The reasonableness of the conclusion reached by the Court of Claims in this case is obvious when it is considered that the most important factor for the surety's determination when entering upon its obligation is whether or not the contract price is fairly adequate to enable the contractor to complete his performance. If it appears that the contract price is wholly inadequate, the surety would foresee failure and decline to give bond. The surety's risk is calculated on the basis of this being the main risk involved, and not upon an effort to forecast the outcome of all past and future dealings which the contractor may have with the Government. The contention of the Government in this case would have the effect of making the contract price a matter of variable uncertainty and would place upon the surety a hazard far beyond anything which could have been contemplated when the contract was written. It must be borne in mind that all contractors with the Government will

be indebted to it continuously for taxes of all kinds, and some for payments of large amounts under the Renegotiation Act[5] and perhaps for penalties and fines of various kinds which may easily amount to considerable sums. It is the Government's contention that all such items as these may be charged against contract balances earned by a contractor under some unrelated contract and that the surety for that contract may in turn be held for the completion and payment of labor and material bills which the contractor failed to pay. It was obviously considerations such as these which moved the Court of Claims in *Maryland Casualty Company* v. *United States*, 100 C. Cls. 513, to say, at pp. 521-2:

> "The effect of the contract and the bonds is that the contractor promises the Government that it will build the structure, *and* will pay the laborers and materialmen. The Government takes two separate bonds to secure the fulfillment of these promises, since its interest in the first is more physical and direct than in the second. But when the surety pays the laborers and materialmen, it is performing the contract as much as when it completes the building. We see no more reason why the parties should intend that, either under the guise of building a building, or of paying laborers and materialmen, both of which the surety has promised will be done, it should in reality, and because of the ease of bookkeeping, be paying the contractors' taxes or other debts, which it has not promised will be done."

See also *Continental Casualty Co.* v. *City of Pittsburgh*, 68 F. Supp. 805 (D. C. W. D., Pa.).

In the present case, if the Government's contention is sound, the surety would be in a better position if it had written a bond for the unrelated St. Louis Post Office work. It would then have received compensation by way of a premium for the assumption of that risk. The Government's present contention is that this surety must pay that loss

[5] Act of April 28, 1942, 50 U. S. C. App. 1191, as amended.

even though it had no connection with the bid and received no compensation for the assumption of the risk. In other words, the Government proposes to charge the surety with responsibility for every debt of the contractor, whether antecedent or subsequent to the bond.

This Court, in construing the provisions of the Government contract involved in *Prairie State National Bank* v. *United States*, 164 U. S. 227, said, at p. 233:

> "That a stipulation in a building contract for the retention, until the completion of the work, of a certain portion of a consideration, is as much for the indemnity of him who may be guarantor of the performance of the work as for him for whom the work is to be performed; that it raises an equity in the surety in the fund to be created; and that a disregard of such stipulation by the voluntary act of the creditor operates to release the sureties, is amply sustained by authority."

And this rule has been applied in cases involving state agencies where similar bonds have been given to secure completion of the work and payment to labor and material furnishers. In such cases where the state agency has paid out retained percentages with the contractor's authorization after notice of outstanding claims against the surety, the agencies have been held liable to the surety for the amounts thus wrongfully disbursed. In *Claiborne Parish School Board* v. *Fidelity & Deposit Co. of Maryland*, 40 F. (2d) 577 (C. C. A. 5th) it was said, at p. 579:

> "On the contrary, a payment of the balance to the contractor or to the bank, with actual knowledge that there were claims outstanding and unpaid, which the appellee (surety) would be compelled to pay, and that it would have to resort to the fund to be reimbursed therefor, would be a wrongful payment as to appellee. The fund was in the possession of appellant for the joint protection of itself and appellee, and it could not lawfully part with the fund to the bank which had no prior right in it, to the detriment of the appellee which it knew would have occasion to resort to it, to secure reimbursement for amounts appellee would be com-

pelled to pay out under the terms of its bonds by the terms of which the fund also provided for its security in that respect." (parenthetical word supplied)

Similar conclusions were reached in *National Surety Co.* v. *County Board of Education*, 15 F. (2d) 993 (C. C. A. 4th); *United States Fidelity & Guaranty Co.* v. *City of Bristow*, (D. C., E. D. Okla.) 4 F. (2d) 810, *Ft. Worth Independant School Dist.* v. *Aetna Casualty & Surety Co.*, 48 F. (2d) 1, (C. C. A. 5th) cert. den. 284 U. S. 645; *Continental Casualty Co.* v. *City of Pittsburgh*, 68 F. Supp. 805 (D. C., W. D. Pa.) It does not appear that any different result should follow because the Federal Government is involved rather than a State Government or agency.

There can be little question under the authorities but that a private agreement between the contractor and the Government to reduce the contract price without the knowledge of the surety would relieve the surety, if not entirely, at least *pro tanto* from the obligation of its bond. What the Government now proposes is this very step. An offset is accomplished on the fundamental notion that debts are mutual and that the parties are agreed that they may be set-off against one another. The consequence of this is that the Government now tells the surety that it has agreed with the contractor to divert the proceeds of the secured contracts to other ends than payment for labor and material which entered into the performance of the work.

Performance by the surety of the contractor's obligation to pay suppliers of labor and material, the contract provision which retains a portion of the contract price as much for the benefit of the surety as for the Government, spell out an obligation by the Government to pay the balances earned by the surety to it and forbid their application to other debts of the contractor for the convenience of the Government.

2. The Government is Not Entitled to Assert a Set-Off.

The extent of the right of set-off in favor of the United States is shrouded in obscurity. There is no statute which specifically defines the class of cases in which it is to be allowed, or the limits within which it is to be confined. It has been said to be:

> "* * * but the exercise of the common right, which belongs to every creditor, to apply the unappropriated monies of his debtor, in his hands, in extinguishment of the debts due to him." *Gratiot* v. *United States*, 15 Pet. 336 at p. 370.

It has been allowed in cases where the quarrel lay between a claimant and the Government alone, *Barry* v. *United States*, 229 U. S. 47, *John P. Squire Co.* v. *United States*, 90 C. Cls. 276. It has been allowed against an assignee of the claimant, *McKnight* v. *United States*, 13 C. Cls. 292, affirmed 98 U. S. 179, and also in favor of the United States where the debt was due to one of its agencies, *Cherry Cotton Mills, Inc.* v. *United States*, 327 U. S. 536.

But where the debts were not mutual, and third parties had an interest in the claim on the one side but no liability for the offset on the other side, the right to set-off has been denied the Government. In cases where suits were brought to enforce the claims of partnerships, attempts to claim set-offs against individual members of the partnerships were denied. *Boehm* v. *United States*, 20 C. Cls. 142, *Marietta Manufacturing Company* v. *United States*, 61 C. Cls. 122. This is in conformity with the notion that the debts must be mutual to be balanced against one another. The principal is illustrated in *Gray* v. *Rollo*, 18 Wall. 629, where a bankrupt insurance company was the holder of notes signed by Gray. Gray was also a member of a partnership to which the insurance company was indebted upon insurance policies. When the insurance company proceeded to enforce payment of Gray's notes, he raised by way of offset, the claims of his partnership upon the policies. In denying

this defense because of the lack of mutuality of the balancing credits, it was said:

> "The insurance company, so far as appears, took the notes without any reference to the policies of insurance; and Gray Brothers insured with the Company without any reference to the notes. Neither transaction was entered into in consequence of or in reliance on the other; and no agreement was ever made between the parties that the one claim should stand against the other."

In the case at bar, not only did the surety know nothing of the claim now endeavored to be used as the basis of set-off, but it did not even arise until subsequent to the giving of the bonds securing the contract.

In discussing this subject it was said in *Scott* v. *Armstrong*, 146 U. S., 499, at p. 507.

> "The right to assert set-off at law is a statutory creation, but courts of equity from a very early day were accustomed to grant relief in that regard independently as well as in aid of statutes upon the subject.
>
> "In equity, relief was usually accorded, says Mr. Justice Story (Eq. Jur. paragraph 1435), 'where, although there are mutual and independent debts, yet there is a mutual credit between the parties, founded, at the time, upon the existence of some debts due by the crediting party to the other. By mutual credit, in the sense in which the terms are here used, we are to understand, a knowledge on both sides of an existing debt due to one party, and a credit by the other party, founded on, and trusting to such debt, as a means of discharging it.'"

In the case at bar it is obvious that the transactions between the United States and the contractor were in no sense based upon the knowledge of existing debts, or upon the extension of credit based upon that knowledge. On the contrary, the United States took the precaution of obtaining independent security for the performance of each obligation assumed by the contractor, and obviously, the case

does not come within that class where equity permits set-offs because of connections between the demands. The allowance of a right of set-off, under the circumstances of this case, would result in the diversion of the contract funds from the payment of bills for labor and material which created the work, and would deprive the surety of that security to which it is entitled by well recognized authority. Such a result would be inequitable.

The Government seems to proceed on the assumption that its right of set-off is a legal right (Petitioner's brief, p. 38-39). In this, it is mistaken. The statute upon which petitioner relies, as creating a legal right of set-off, R. S. 236,[6] is no more than an organic provision assigning to the General Accounting Office the function of settling and adjusting claims by or against United States. That statute creates no substantive rule to regulate and control adjustments and set-offs to be made by the General Accounting Office. It provides merely that the General Accounting Office shall apply such stubstantive law as may be available for these purposes. The propositions which the General Accounting Office must apply in effecting set-offs are equitable in nature.

Since the debts are not mutual, and because it would be inequitable to balance them against one another to the damage of the surety, no case for an offset is made. It is submitted that the Court of Claims was correct in rejecting the contention of the General Accounting Office on this point.

3. The Equitable Doctrines Which Have Been Applied in These Cases Support the Surety's Position.

A wealth of authority in the Circuit Courts of Appeal has established beyond any question the right of a surety to be reimbursed out of the contract balances where it has either completed the work, or paid suppliers of labor and material. This result has been reached by awarding to the surety subrogation to the rights of the United States, to

[6] App. p. 25.

the rights of the labor and material furnishers or to the rights of the contractor and by declaring the contract proceeds subject to an equitable lien. The decisions are substantially unanimous in result, although the theories assigned to support them vary according to the necessities of individual cases. It is the purpose of this discussion to show that the decisions based upon equitable principles are in entire consonance with the proposition advanced by the respondent here, that it has a direct legal right to these contract proceeds.

The first case to come before this Court involving the rights of the surety upon a defaulted Government contract was *Prairie State National Bank* v. *United States*, supra. In that case the surety had completed the work after the contractor's default. It was held that the surety was entitled to subrogation *to the rights of the United States*, and that its subrogation must be considered as arising from and relating back to the date of the original contract. It was concluded that the surety became entitled to resort to the securities and remedies which the United States, the creditor, were capable of asserting against the contractor, and that one of such remedies was the right arising from the original contract, to appropriate the monies retained for the reduction of damage.

In re Scofield Co., 215 Fed. 45 (C. C. A. 2nd) presents an instance where the contractor completed the work, but failed to pay furnishers of labor and material. The retained percentages had come into the hands of the contractor's trustee in bankruptcy. The surety paid the claims and then asserted its right to the contract balance. The Court said, at p. 47:

> "The question thus presented is whether, under the circumstances stated, the surety of the bankrupt contractor who has paid the claims of the laborers and materialmen has any equity in this so-called reserved fund which it can assert to the exclusion of the general creditors."

and again, at p. 50:

"We are unable, however, to see that any real difficulty exists as to the rules which govern the facts of this case. It is not disputed that the claims which the Fidelity Company has satisfied are claims which it was the duty of the Scofield Company to pay. In making the payments it did the Fidelity Company discharged obligations due from the Scofield Company for the performance of which the Fidelity Company was bound under the obligation of its suretyship. When the Fidelity Company assumed the obligation of suretyship its equity at once commenced with its obligation to see that the Scofield Company duly performed all the obligations which the contract with the Government imposed upon it, including its obligations to promptly pay the laborers and materialmen. The Supreme Court in *Prairie State Bank* v. *United States*, 164 U. S. 227, 233, 17 Sup. Ct. 142, 41 L. Ed. 412 (1896), held that a stipulation in a building contract for the retention until the completion of the work of a certain portion of the consideration is as much for the indemnity of him who may be quarantor of the performance of the work as for him for whom the work is to be performed, and that it raised an equity in the fund to be created. In accordance with this doctrine the equity of the Fidelity Company in this reserved fund cannot be successfully questioned. And the fact is quite immaterial that the contract which the Scofield Company made with the government provided simply for the retention of the fund until the completion of the work. A similar provision existed in the contract in the Prairie State Bank Case, but that fact did not prevent the Supreme Court from regarding the reserved fund as withheld for the benefit of the surety, as well as for the protection of the government. The doctrine of that case was reasserted by the Supreme Court in *Henningsen* v. *United States Fidelity & Guaranty Co.*, 208 U. S. 404, 28 Sup. Ct. 389, 52 L. Ed. 547 (1908). These cases show that the equity of the surety who pays the debts arising under the contract will take precedence of any assignment of funds due from the Government made by the contractor. *A fortiori* the equity of the surety must take precedence of the general creditors."

Henningsen v. *United States Fidelity & Guaranty Company*, 208 U. S. 404, developed out of a situation where the contractor had completed the work but had failed to pay furnishers of labor and material. They were paid by the surety pursuant to its Heard Act[7] bond, but the right to the contract proceeds was contested by the contractor's assignee. In holding that the surety was entitled to subrogation and to reimbursement from the contract proceeds this Court said, at p. 410.

> "The guaranty company was surety on that contract. Its stipulation was not merely that the contractor should construct the buildings, but that he should pay promptly and in full all persons supplying labor and material in the prosecution of the work contracted for. He did not make this payment, and the guaranty company, as surety, was compelled to and did make the payment. Is its equity superior to that of one who simply loaned money to the contractor, to be by him used as he saw fit, either in the performance of his building contract or in any other way? We think it is. It paid the laborers and materialmen, and thus released the contractor from his obligations to them, and to the same extent released the Government from all equitable obligations to see that the laborers and supplymen were paid. It did this not as a volunteer, but by reason of contract obligations entered into before the commencement of the work."

See also:

Hardaway v. *National Surety Company*, 211 U. S. 552;

Belknap Hardware & Mfg. Co. v. *Ohio River & Contract Co.*, 271 Fed. 144 (C. C. A. 6th);

Morgenthau v. *Fidelity & Deposit Co. of Maryland*, 94 F. (2d) 632.

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[7] App. p. 26.

It has been said:

> "That the equitable lien thus recognized arose at the time of the execution of the bond and was superior to the assignment to the appellant bank is decided by the great weight of authority" *Exchange State Bank* v. *Federal Surety Co.* 28 F. (2d) 485 (C. C. A. 8th), at p. 488.

In another instance where both the contractor and the sureties had become insolvent, furnishers of labor and material were recognized as having a right of lien upon the contract proceeds, and that right was enforced at their own instance, *Philadelphia National Bank* v. *McKinlay*, 63 App. D. C. 296, 72 F. (2d) 89, cert. den. 293 U. S. 583.

In *American Bonding Co.* v. *Central Trust Co.*, 246 Fed. 400 (C. C. A. 7th), the contractor had become bankrupt. The surety had given a bond in the amount of $1,250.00, conditioned for payment of persons furnishing labor and material to the work. Of the contract fund, $2,000 had come into the hands of the trustee in bankruptcy. It was said by the Court at p. 402:

> "The $2,000.00 fund in the hands of the trustee in bankruptcy stands charged with the same equities as to the materialmen and the surety upon the bond who had paid the materialmen as it was bound to do, as when it was undistributed in the hands of the United States. Whatever rights were acquired by reason of the contractor's assignment and payment thereon by the United States, were subject to the right of the materialmen and surety on the bond to have their claims paid in full. Henningsen v. United States Fidelity & Guaranty Co., 208 U. S. 404, 410, 28 Sup. Ct. 389, 52 L. Ed. 547.
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> "That the surety, on the payment of labor and material claims, was subrogated and that its equity attached as of the date of the bond, and that a mere volunteer's rights would be subject to those of the surety who pays the labor and material bills, was clearly laid down in Prairie State Bank v. United

States, 164 U. S. 227, 240; 17 Sup. Ct. 142, 41 L. Ed. 412. This was approved in Henningsen v. United States, supra.

> "In the case at bar, the assignee of the contractor stands in the position of a mere volunteer and is not therefore entitled to the benefit of the doctrine of subrogation. Under the authorities quoted, the materialmen and the surety in the case at bar have a prior right to the extent of their claims in the fund so in the hands of the trustee in the nature of an equitable lien: It precedes the rights of assignees of the contractor and also those of the general creditors.
>
> "There can be no doubt but that the trustee in bankruptcy took the fund, as above stated, charged with the payment of claims of the materialmen and of the surety on the bond as prior liens thereon and with the duty of making distribution of said several sums so due thereon."

See also *Moran* v. *Guardian Casualty Co.*, 64 App. D. C. 188, 76 F. (2d) 438, from which the Court of Claims quoted at length in its opinion (R. 21).

The equities which are enforced in favor of the surety extend as well to current or progress payments as to retained percentages reserved under the contract. It was said in *Lacy* v. *Maryland Casualty Company*, 32 F. (2d) 48 (C. C. A. 4th) at page 51:

> "The rule is well settled that, independently of assignment, the surety on a contractor's bond, who completes the contract on default of the principal, is subrogated to the rights of the obligee, and, to the extent necessary to reimburse himself, has an equity in the funds due the contractor, which is superior to that of a mere assignee." Citing cases. * * *
>
> "The question arises whether this superior equity of the surety extends to the current estimates payable under the contract or merely to the retained percentage. We think that it extends to both. The equity arises because of the obligation of the surety to perform the contract of the principal. Upon his performance of this contract, equity subrogates him to all rights of the

obligee as against the principal. Now the obligee, upon default of the principal, is without doubt entitled to apply all monies unpaid toward the performance of the contract, ignoring any assignments by the principal; and it necessarily follows that the surety upon performing the contract, being subrogated to the rights of the obligee, is entitled to the monies unpaid so far as necessary to reimburse his loss. If the surety, instead of performing the contract, elects to pay damages, it can be held for no more than the amount which the obligee is compelled to pay to complete the work over and above the amount which it has on hand at the time of the principal's default, for this is all the damage that the surety sustains. But when this happens the surety receives the benefit of the unpaid current estimates as well as the retained percentages. Equity, of course, will not place him in worse position where he performs the contract of the principal in accordance with his obligation than where he elects to respond in damages."

The fund which this Court awarded to the furnishers of labor and material in *Martin* v. *National Surety Company, supra,* consisted of both progress payments and retained percentages.

Nor does the division of the surety's liability into two bonds, one conditioned for completion of the work, and the other for payment of labor and material furnishers affect the result. In *Riverview State Bank* v. *Wentz*, 34 F. (2d) 419 (C. C. A. 8th), a contractor with a state agency had given two such bonds required by two state statutes, but had failed to pay furnishers of labor and material. They were paid by the surety on that bond. The Circuit Court of Appeals held that the surety was entitled to subrogation and that its right was superior to that of an assignee of the contractor. It was said (p. 421):

> "Obviously, it makes no difference in the law that there was but one statute, one bond and one surety, in the Henningsen Case; while here there are two statutes, two bonds, and but a single surety. The bond here for completion of the work is nowise directly in question or

in issue. The case would be the same if the latter bond never had been executed. Nothing seems more obvious, or plainer than that the mere adventitious fact that the Guaranty Company happens to be the surety on both of the bonds made in this case, cuts no earthly figure in the law of the case."

Thus it is seen that equity has recognized and freely enforced the rights of the surety and of the labor and material furnishers to the fund which constitutes the contract proceeds.* Nor is there any reason why when the work is finished and furnishers of labor and material have been paid by the surety, that the Government should not, in full recognition of its liability pay the agreed price therefor to the surety, even though it may have taxes and other unrelated claims due it from the contractor.

4. Comments on the Government's Brief.

The Government urges that greater convenience will result if the surety is required to sue the contractor. (Petitioner's brief, p. 20) It overlooks the fact that the surety and the contractor have already engaged in litigation in the very proceeding in which the respondent was appointed receiver. It is quite obvious that neither the Government nor the surety entertain prospects of satisfying their claims except from the fund here involved. Although there is no indication that the contractor is insolvent, the record shows plainly that it failed to pay numerous persons furnishing labor and material under its contracts, and likewise failed to pay the Government's claim on the St. Louis job and that none of these items have been paid by the contractor down to this time. Relief in matters of this kind has never been predicated so much upon insolvency as upon the recognition that the surety had a special interest in the con-

* The Government's reference to conflict of decisions in this field (Petitioner's Brief, p. 28) will be found to relate principally to cases involving local law or contracts and bonds having provisions which controlled the decision of individual cases.

tract proceeds which was entitled to the protection of the courts.

The Government suggests, in its brief, (Petitioner's brief, p. 22) that the respondent is a special receiver for the fund and as such must rely on the rights of the contractor thereto. It is entirely apparent from the order of the District Court, appointing respondent (R. 5-6) that the receiver was appointed for the benefit of the surety, and that the proceeds of the receiver's collection will go for the surety's reimbursement. Under those circumstances, the receiver succeeds to, and is entitled to enforce all claims which the surety might have against the contract proceeds. *Samuel Olson and Company v. Voorhees, et al.*, 292 Fed. 113 (C. C. A. 3d); *Hart v. Barney & Smith Mfg. Co.*, 7 Fed. 543 (C. C. D., Ky); *Bell v. New York Safety Steam Power Co.*, 183 Fed. 274 (C. C., S. D. N. Y.) *Hamor v. Taylor-Rice Engineering Co.*, 84 Fed. 392 (C. C., Del.)

The Government has urged that a surety cannot become subrogated to the debt which it pays unless it pays the whole debt, or it is otherwise satisfied (Petitioner's brief, p. 34) and endeavors to apply that rule to the case in hand. That rule, as illustrated by *United States v. National Surety Company*, 254 U. S. 73, and *Jenkins v. National Surety Company*, 277 U. S. 258, applies only to the *particular* debt which the surety has secured. That rule has never been extended to the point of saying that the surety could not be subrogated to the debt which it had paid in full as long as the creditor had any other claims against the debtor. In the case at bar the Government has no claim in connection with the contracts which the surety bonded since they have been satisfied in full. Accordingly, *United States v. National Surety Company, supra*, raises no barrier to the allowance of subrogation.

Where security is pledged for the obligation which the surety has undertaken, the creditor is not free to avail himself of that security for the payment of other obligations due him by the debtor. In *City National Bank of*

Ottawa v. *Dudgeon*, 65 Ill. 11, the debtor owed the bank several obligations among which was a note secured both by a mortgage and a surety. The surety paid the note and thereafter the bank endeavored to satisfy other of its claims against the debtor out of the mortgaged land. The right to do this was denied by the Court which held the surety entitled to subrogation to the security of the creditor for the particular debt which the surety had paid. This doctrine is summarized in Pomeroy's Equity Jurisprudence 5th Ed. (Symons) Vol. 4, ¶ 1419, p. 1075, as:

> "It necessarily follows from the surety's right of subrogation that the creditor cannot, without the surety's assent, surrender, give up, release, or discharge any such securities, or render them in any way unavailable to the surety, either by his own acts or omissions. If he does so, the surety's liability is thereby discharged, wholly or partially, as the case may be."

Reference is made in the Government's brief (p. 38-39) to the fact that the Treasury Department as well as the General Accounting Office have followed a practice of making set-offs for many years past. There can be no quarrel with the accuracy of this statement but on the other hand there is no line of precedents under which either of those offices may invade contract funds to the prejudice of sureties which had either completed the work or paid labor and material claims. And the Government admits that the decisions of the courts are adverse to it on this point. It is quite unlikely that the Government has ever attempted to make an offset of unrelated items against progress payments in the early stages of the work, although this would be in conformity with the position the Government now takes.

CONCLUSION.

The money which is here involved represents contract proceeds amounting to no more than, and as to some contracts less than, the amount of claims of unpaid labor and material furnishers. The money here involved was earned

by the surety which paid for this much of the labor and material which created the work. To the same extent the contractor defaulted under both its contract and bond and forfeited its right to further contract payments. The money here involved is in reality that of the surety.

The whole implication of the transaction is that the contract proceeds were a fund to be devoted to the construction of the work. The Government is not free to divert these monies to the payment of its unrelated debts, not only because the clear intention of the parties was otherwise, but also because the Government has the same responsibilities with respect to its contracts as a private person. *Perry v. United States*, 294 U. S. 330.

> "Punctilious fulfillment of contractual obligations is essential to the maintenance of the credit of public as well as private debtors." *Lynch v. United States*, 292 U. S. 571, at p. 580.

It is illogical and absurd that the surety for one contract should in effect become a surety for all of the contractor's debts to the government as the direct result of its coming forward and performing those obligations of the contractor which it guaranteed. And this without regard to whether the unrelated transaction long antedated or followed the giving of the bond. Such a result can be achieved only by attaching more importance to bookkeeping than to substance.

Not only this, but clearly there is a want of mutuality between the claim of the Government on the one hand arising from the contractor's failure to paint the St. Louis Post Office and the claim of the surety on the other hand to receive the contract proceeds to the extent that it fulfilled the contractor's obligation to its supplymen. There can be no presumption that the parties intended to allow the credits and debts arising out of the independent transactions to be credited against one another. On the contrary, the taking of security in connection with each transaction indicates that it was the intention of the Government, the

contractor, and the surety to treat each transaction as independent and unrelated.

It is submitted that in right and justice the fund which represents the completed work should be awarded to the surety which fulfilled the requirements of the contracts and bonds by paying for the labor and materials used in the work.

Respectfully,

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APPENDIX.

1. R. S. 236 is as follows:

> All claims and demands whatever by the Government of the United States or against it, and all accounts whatever in which the Government of the United States is concerned, either as debtor or creditor, shall be settled and adjusted in the General Accounting Office. (R. S. 236; June 10, 1921, c. 18, 305, 42 Stat. 24; 31 U. S. C. 71)

2. Pertinent parts of the Miller Act which directs the contracting agency to obtain the completion and material supplier's bonds are as follows:

> Before any contract, exceeding $2,000 in amount, for the construction, alteration, or repair of any public building or public work of the United States is awarded to any person, such person shall furnish to the United States the following bonds, which shall become binding upon the award of the contract to such person, who is hereinafter designated as "contractor":
>
> (1) A performance bond with a surety or sureties satisfactory to the officer awarding such contract, and in such amount as he shall deem adequate, for the protection of the United States.
>
> (2) A payment bond with a surety or sureties satisfactory to such officer for the protection of all persons supplying labor and material in the prosecution of the work provided for in said contract for the use of each such person. Whenever the total amount payable by the terms of the contract shall be not more than $1,000,000 the said payment bond shall be in a sum of one-half the total amount payable by the terms of the contract. Whenever the total amount payable by the terms of the contract shall be more than $1,000,000 and not more than $5,000,000, the said payment bond shall be in a sum of 40 per centum of the total amount payable by the terms of the contract. Whenever the total amount payable by the terms of the contract shall be more than $5,000,000 the said payment bond shall be in the sum of $2,500,000.

* * * * *

(Aug. 24, 1935, c. 642, 1; 49 Stat. 793; 40 U. S. C. 270a et seq.)

3. Pertinent parts of the Heard Act which preceded the Miller Act are as follows:

> Any person or persons entering into a formal contract with the United States for the construction of any public building, or the prosecution and completion of any public work, or for repairs upon any public building or public work, shall be required, before commencing such work, to execute the usual penal bond, with good and sufficient sureties, with the additional obligation that such contractor or contractors shall promptly make payments to all persons supplying him or them with labor and materials in the prosecution of the work provided for in such contract; and any person, company, or corporation who has furnished labor or materials used in the construction or repair of any public building or public work, and payment for which has not been made, shall have the right to intervene and be made a party to any action instituted by the United States on the bond of the contractor, and to have their rights and claims adjudicated in such action and judgment rendered thereon, subject, however, to the priority of the claim and judgment of the United States. If the full amount of the liability of the surety on said bond is insufficient to pay the full amount of said claims and demands, then, after paying the full amount due the United States, the remainder shall be distributed pro rata among said interveners.
>
> * * * * *

(Aug. 13, 1894, c. 280, 28 Stat. 278; Feb. 24, 1905, c. 778, 33 Stat. 811; Mar. 3, 1911, c. 231, 291, 36 Stat. 1167; 40 U. S. C. 270)

SUPREME COURT OF THE UNITED STATES

No. 847.—October Term, 1946.

The United States, Petitioner, *v.* The Munsey Trust Company of Washington, D. C., Receiver.	On Writ of Certiorari to the Court of Claims.

[June 23, 1947.]

Mr. Justice Jackson delivered the opinion of the Court.

This case presents a problem arising out of contracts for public building construction and repair. The rights *intersese* of contractor, surety, assignees and government have been productive of much litigation, but we have not heretofore had to decide whether percentages retained pursuant to contract by the United States may be subjected to its set-off claims despite the claims of a surety who has paid laborers and materialmen.

In May and July, 1940, six contracts were made between the United States and the Federal Contracting Corporation, in which the corporate contractor agreed to paint and repair certain federal buildings. Each contract conformed to the requirements of statute, 49 Stat. 793, 40 U. S. C. § 270a, *et seq.*, by providing for two surety bonds, one conditioned on the completion of the work within the contract period, and the other on the payment of those furnishing labor and material to the contractor. The Aetna Casualty and Surety Company signed those bonds, each of which assigned to it the contractor's claims against the government for sums due on the contracts whenever the surety should be compelled by default of the contractor to fulfill its obligations.[1]

[1] These assignments were of course invalid against the United States, R. S. § 3477, 31 U. S. C. § 203; *Martin* v. *National Surety Co.*, 300 U. S. 588, but they enable the surety to prevail over the contractor if there is contest between them.

The work was completed by the contractor apparently in 1940, and accepted by the government. The surety therefore was not called upon to make good the promise of the performance bonds. But the contractor did not pay $13,065.93 owed to persons who had supplied labor and material for performance of five of the six contracts. This indebtedness the surety paid between April and September, 1941 as the payment bonds obliged it to do.

Under the customary terms of its contracts, the government had retained percentages of the progress payments due to the contractor. This retained money, on acceptance of the work, amounted to $12,445.03, but it was not disbursed. On October 18, 1940, the Federal Contracting Corporation submitted a bid to the United States for another painting job, in St. Louis. That bid was accepted, but the contractor then failed to enter into contract for the work. Another contractor painted the building for a price which left the government considerably more out-of-pocket than it would have been had Federal undertaken performance at its bid price. It is undisputed that $6,731.50 is the amount of damages sustained by the government after it had applied the contractor's deposit of $415.00 in reduction.

Almost inevitably, court process was begun to untangle claims to the money the United States still owed on the six contracts. A stockholder of Federal asked the United States District Court for the District of Columbia to appoint a receiver [2] to collect the money. The Aetna Casualty and Surety Company was made a party to that action. Respondent here, the Munsey Trust Company, was appointed receiver with directions to demand and

[2] Such proceedings to appoint a receiver in the District of Columbia are for the purpose of taking possession of a fund or property and to prevent its loss or dissipation. Insolvency is not a necessary allegation, *Houston* v. *Ormes*, 252 U. S. 469, and there is no claim in this case that the contractor is insolvent.

authority to receive from the United States the proceeds of the six contracts. The order of appointment also recited that "the proceeds of all collections made by the Receiver pursuant to this order shall be held for the reimbursement of the defendant The Aetna Casualty and Surety Company for expenditures made by it in the payment of furnishers of labor and material under the several contracts of the Federal Contracting Corporation."

On demand by the receiver for the amounts due, the General Accounting Office deducted the government's claim of $6,731.50 and paid over $5,713.53. Aetna, by letter to the Comptroller General, protested the government's settlement by set-off and asserted its right to an additional $3,568.23.[3] The receiver also protested the set-off and demanded $3,143.23 for reimbursement of the surety. It relied upon *Maryland Casualty Co. v. United States*, 100 C. Cls. 513, 53 F. Supp. 436. The Acting Comptroller General declined to follow the opinion of the Court of Claims, in the absence of ruling by this Court, and rejected the protests. When the receiver reported its efforts to the district court, it was ordered to turn over to the surety the money collected, less $500. That sum was for prosecution of suit in the Court of Claims for the recovery of whatever other moneys "may be due under the contracts of the Federal Contracting Corporation." This action was begun, and the Court of Claims gave judgment for $3,568.23 to respondent. We granted the government's petition for certiorari because of the importance and novelty of the question and the cumulative effect of *Maryland Casualty Co. v. United States, supra*, and the decision below. — U.S. —.

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[3] The surety did not and could not claim the whole amount retained by the government. The payments for which it was liable and which it paid, on two of the contracts exceeded, and, on the other four, were less than, the amounts retained on each particular contract.

In these cases, it is usual for the rights relied upon to be largely derivative or subrogated ones. Decision will be attended with unnecessary confusion and difficulty if it is not clear whose rights are being asserted and who claims them. The Court of Claims treated this case as though the surety were plaintiff. But the district court directed the receiver to bring the suit. Its order of appointment made it the representative of Federal Contracting Corporation, although the sums it was to collect were to be held for the reimbursement of Aetna. The second order authorized this action to collect whatever other money might be held to be due under the six contracts which the government would not voluntarily pay. Certainly, the receiver sued at least in the right of Federal, but since its efforts were directed to be for the benefit of Aetna, it might assert the surety's rights also. *Samuel Olson & Co.* v. *Voorhees,* 292 F. 113, 115.

If the right of the United States to make the set-off were opposed only by the claims of the contractor, the case would present no difficulty. The government has the same right "which belongs to every creditor, to apply the unappropriated moneys of his debtor, in his hands, in extinguishment of the debts due to him." *Gratiot* v. *United States,* 15 Pet. 336, 370; *McKnight* v. *United States,* 98 U. S. 179, 186. More than that, federal statute gives jurisdiction to the Court of Claims to hear and determine "All set-offs, counterclaims, claims for damages, whether liquidated or unliquidated, or other demands whatsoever on the part of the Government of the United States against any claimant against the Government in said court . . ." Judicial Code § 145, 28 U. S. C. § 250 (2). This power given to the Court of Claims to strike a balance between the debts and credits of the government, by logical implication gives power to the Comptroller General to do the same, subject to review by that court. Insofar as the suitor in the Court of Claims as-

serted the contractor's title to the sum in dispute, that court was under statutory duty to recognize the undisputed claim for damages of the United States. *Cherry Cotton Mills, Inc.* v. *United States*, 327 U. S. 536.

But the surety urges that it is subrogated also to the rights of laborers and materialmen whom it paid and of the United States. From *Prairie State Bank* v. *United States*, 164 U. S. 227, to *American Surety Co.* v. *Sampsell*, 327 U. S. 269, we have recognized the peculiarly equitable claim of those responsible for the physical completion of building contracts to be paid from available moneys ahead of others whose claims come from the advance of money. But in all those cases, the owner was a mere stakeholder and had no rights of its own to assert. Respondent tells us that here the United States is in the same position and that as a general creditor, it has no more right to the money which it holds than does any other general creditor of the contractor.

At the time demand for payment was made by the receiver, the claim of the United States on the St. Louis contract was extant for some time. The disbursing officers, therefore, did not concede that they held the entire amount of the retained percentages for distribution to the contractor or others. And one whose own appropriation and payment of money is necessary to create a fund for general creditors is not a general creditor. He is not compelled to lessen his own chance of recovering what is due him by setting up a fund undiminished by his claim, so that others may share it with him. In fact, he is the best secured of creditors; his security is his own justified refusal to pay what he owes until he is paid what is due him.

But the infirmity in respondent's case goes deeper. If the United States were obligated to pay laborers and materialmen unpaid by a contractor, the surety who discharged that obligation could claim subrogation.

But nothing is more clear than that laborers and materialmen do not have enforceable rights against the United States for their compensation. *Cf. H. Herfurth, Jr., Inc.* v. *United States*, 89 Ct. Cls. 122; see *Schmoll* v. *United States*, 105 Ct. Cls. 415, 455; *Maryland Casualty Co.* v. *United States*, 53 F. Supp. 436, 440. They cannot acquire a lien on public buildings, *Hill* v. *American Surety Co.*, 200 U. S. 197, 203; *Equitable Surety Co.* v. *McMillan*, 234 U. S. 448, 455, and as a substitute for that more customary protection, the various statutes were passed which require that a surety guarantee their payment. Of these, the last and the one now in force is the Miller Act under which the bonds here were drawn.

The surety says, nevertheless, that the laborers and materialmen may have a lien, or something in the nature of a lien on the retained percentages. Its argument runs into logical difficulties. For it asserts that the moneys are retained by the government as much for assurance that the contractor will perform his contract by paying the laborers and materialmen as by completing the work on time. It is said to follow that so long as they remain unpaid, the contractor may not demand payment and the government would be justified in refusing to disburse the retained percentages.[4] In that case, how may the laborers and materialmen have a lien upon money which the United States may legally keep? Surely it is not intended that the laborers and materialmen may claim payment of that which is not due to the contractor. We are aware that the laborers and materialmen have been paid, so that by no interpretation of the contracts between government and contractor

[4] If the money is retained only to assure performance of the work, then the contractor might compel payment when the work is accepted. In that case, the surety's argument fails, since obviously, before paying, the government might set off claims against the contractor.

can there be restrictions on paying out the money retained. It is said that it was the surety's payment of those claims which released the asserted contract restrictions. In relying on the rights of the laborers and materialmen, however, the surety must establish that those rights existed before their claims were paid. For it is elementary that one cannot acquire by subrogation what another whose rights he claims did not have. Once the laborers and materialmen have been paid, either by contractor or surety, they have no rights in any fund. If before they are paid, the fund to which they are said to be entitled to look is unavailable for the very reason that they are unpaid, the surety relies on nothing when it relies on those nonexistent "rights." One who rests on subrogation stands in the place of one whose claim he has paid, as if the payment giving rise to the subrogation had not been made. See *Aetna Life Insurance Co.* v. *Middleport*, 124 U. S. 534, 548. He cannot jump back and forth in time and present himself at once as the unpaid claimant and again, under the conditions as they have changed because payment was made.

We need not decide whether laborers and materialmen would have any claim to the retained percentages, if both contractor and surety failed to pay them. Even if they do, certainly these would be rights to which the surety could not be subrogated for by hypothesis it would have done nothing to earn subrogation.

The surety has yet another party whose rights it would claim, if it cannot prevail by substitution for contractor or laborers and materialmen. This contention too was sustained by the Court of Claims when it said that the rights of the United States devolved upon the surety, because of its payments. We are told that the United States retained the money to assure performance of all the obligations of the contractor, and that the surety is entitled to apply that security to indemnify itself for

performing one of those obligations. This is by analogy to the rule that an obligee, as against a surety, may not apply security in satisfaction of debts ~~other~~ than the one it secures. See 4 Pomeroy, Equity Jurisprudence (5th ed.) 1075. But although we have assumed, for the purposes of another argument, that assurance that laborers and materialmen will be paid is one of the reasons for retaining the money, it seems more likely that completion of the work on time is the only motive. *California Bank* v. *United States Fidelity & Guaranty Co.*, 129 F. 2d 751; see *Schmoll* v. *United States*, 105 C. Cls. 415, 455; *Maryland Casualty Co.* v. *United States*, *supra* at 439. It is hardly reasonable to withhold money in order to assure payments which perhaps can be made only from the money earned. In any event, we are not prepared to apply law relating to security to unappropriated sums which exist only as a claim.

Finally, the surety by reference to the *Maryland Casualty* case, *supra*, suggests that it has rights of its own in the money which the government retained. It argues that the implication of the several contracts among government, contractor and surety was that the moneys earned under the repair contracts would be available to pay claims arising under each job. However, if statute did not require a surety, there could be no question that the government would have the right of set-off. Respondent's contention then comes to this: that by requiring the contractor to furnish assurances that he will perform his obligations to laborers and materialmen, the government has deliberately decreased the ordinary safeguards it would have had to enforce the contractor's obligations to it. We see nothing in the words of the contract or the statute to lead us to this conclusion. On the contrary, the statutory provisions requiring a separate bond for payment of laborers and materialmen were enacted for their benefit, not to the detriment of the government.

It is the surety who is required to take risk. We have no warrant to increase risks of the government.

Respondent argues that if the work had not been completed, and the surety chose not to complete it, the surety would be liable only for the amount necessary to complete, less the retained money. Moreover, if the surety did complete the job, it would be entitled to the retained moneys in addition to progress payments. The situation here is said to be similar. But when a job is incomplete, the government must expend funds to get the work done, and is entitled to claim damages only in the amount of the excess which it pays for the job over what it would have paid had the contractor not defaulted. Therefore, a surety would rarely undertake to complete a job if it incurred the risk that by completing it might lose more than if it had allowed the government to proceed. When laborers and materialmen, however, are unpaid and the work is complete, the government suffers no damage. The work has been done at the contract price. The government cannot suffer damage because it is under no legal obligation to pay the laborers and materialmen. In the case of the laborers' bond, the surety has promised that they will be paid, not, as in the case of performance bond, that work will be done at a certain price. The law of damages is therefore not pertinent to the payment bond.

We hold that the government properly used its right to set off its independent claim and the judgment below must be

Reversed.

MR. JUSTICE BURTON dissents.

MR. JUSTICE DOUGLAS took no part in the consideration or decision of this case.